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Bernard V. Brady

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Bernard V. Brady, *Satisfaction of Dissenting Claims in Reorganization Schemes Under Section 77B*, 19 Marq. L. Rev. 106 (1935).
Available at: <http://scholarship.law.marquette.edu/mulr/vol19/iss2/4>

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SATISFACTION OF DISSENTING CLAIMS IN REORGANIZATION SCHEMES UNDER SECTION 77B *

BERNARD V. BRADY

IN DEALING with rights of dissenting landlords and secured creditors under section 77B of the Bankruptcy Act,¹ it is necessary to assume the presentation of a plan of reorganization either by the debtor or by creditors, which is to be confirmed, and the operation of which will necessitate dealing with the rights of a lessor or secured creditor either under the plan or independent of the plan. Creditors include, for the purposes of the section, all holders of claims of whatever character against the debtor or its property; and claims include debts, securities other than stock, and liens or interests of whatever character. A test for determination of whether the interests of a claimant are affected by the plan of reorganization is provided by the declaration that no creditor shall be deemed affected by a plan of reorganization unless the plan shall affect his interests materially and adversely.

Under Section 77B a plan of reorganization is defined as one which shall include provisions modifying or altering the rights of creditors generally or of any class of them, secured or unsecured. The Act provides that in respect to each class of creditors of which less than two-thirds in amount shall accept the plan, the plan shall provide adequate protection for the realization by them of the value of their interests, claims, or liens if the property affected by their interests, claims, or liens is dealt with by the plan; and that the plan may provide such protection in any one of the following ways, namely: (1) By transfer or sale of the property subject to their interests, claims, or liens or by the retention of the property by the debtor subject to such interests, claims, or liens; or (2) By a sale, free of such interests, claims and liens, at not less than a fair upset price, and the transfer of the claims or liens to the proceeds of the sale; or (3) By appraisal and payment in cash of the value of such claims or liens, or, at the objecting creditors' election, payment of such value in securities of the kind allotted to that class of claimants; or by any method which will, in the opinion of the judge, consistent with the circumstance of the particular case, equitably and fairly provide that protection. The Act permits the rejection of contracts of the debtor which are executory in whole or in part, including unexpired leases, except contracts in the public authority.

*This paper was read at a meeting of the Milwaukee County Bar Association, January 5, 1935.

¹ Chapter 424, s. 1, 48 Stat. (1934), 11 U.S.C.A. 207.

Whether a landlord's claim for damages based on loss of future rentals resulting from termination of the lease through a lessee's bankruptcy, was a provable claim in bankruptcy entitling the lessor to share in the bankrupt's assets, was long a matter of controversy. It was finally set at rest by a rather recent decision of the United States Supreme Court in which it was held that such claims were not provable in bankruptcy.² Apparently as a result of that decision Section 63 of the Bankruptcy Act defining provable claims was amended to allow landlords to prove such damages, but not exceeding the present value of the amount of rent which would have accrued for the next ensuing year under the lease.³ A comparable provision has been carried over into the corporate reorganization section, by permitting the landlord to prove his damages for such a termination of the lease, but not exceeding an amount in excess of the present value of rent which would have accrued under the lease for the next ensuing three years.

When a lease held by the debtor has been rejected there is merely presented the landlord's claim for past rent and for damages in respect of which, if he should be so fortunate as to hold security, he would stand in the class of secured creditors much as any other creditor holding security, or if without security would fall into the class of unsecured creditors with whom we are not now concerned. In either event, his situation would not present problems peculiar to landlords dissenting from a plan of reorganization for whom protection must be afforded. It is only in those instances in which the lease is proposed to be continued, rather than rejected, that there are presented problems of the rights peculiar to the lessor in relation to a plan of reorganization.

The question arises: when is a lessor secured? The answer—almost always. It is almost universal that the lease or the state law, or both, give the lessor at the minimum the right to terminate the lease for default in payment of rent. So long as it is proposed to continue the lease by the plan of reorganization, the lessor would seem to be in position to assert that he must be dealt with as a secured creditor,—one who has made a grant or demise of land for a term of years reserving a right of termination for failure of the lessee to pay the rent. As a practical matter it is probable that the question will not frequently arise whether, of itself, the right of the lessor to terminate for non-payment of rent requires the lessor to be classified as a secured claimant. The instances in which it will be desired by the debtor to continue a lease will undoubtedly be ones in which the lease has a considerable term to run and

² *Manhattan Prop. v. Irving Tr. Co.*, 291 U.S. 320, 54 Sup. Ct. 385, 78 L.Ed. 825 (1934).

³ Chapter 424, s. 4 (a), 48 Stat. (1934), 11 U.S.C.A. 103 (a), (7).

represents an investment of capital by the debtor, or has such peculiar relation to continuing the debtor's business, as would prompt the debtor to continue the lease as part of the plan of reorganization; and in practically all such instances where the debtor is economically tied to the lease through peculiar relations to his business or through having made substantial investment in improvements on the leased premises, it will be found that the lessor is usually secured by a first lien reserved on the lessee's estate, and by right of forfeiture of the lessee's interest in building improvements through terminating the lease; and in some states the landlord is given a lien on all of the tenant's chattels which may be on the leased premises.

Lessors and secured creditors dissenting from a plan of reorganization will be brought into relation with the plan in either one of two ways: as objectors when two-thirds of the claimants of their class have consented; or as objectors when two-thirds of the claimants of their class have not consented to the plan.

In the first instance the objector has the plan forced upon him against his wishes by reason of the fact that two-thirds of the claimants of his class have assented to the plan. In the second instance, he is entitled to adequate protection for the realization of the value of his lien or security, in the manner which has been referred to.

The former provision may seem to furnish a rather universal and sweeping method of dealing with secured claimants, and give rise to apprehension on the part of a secured landlord or claimant as to his being drawn, over his objection, into a plan of reorganization merely because two-thirds of the others of his class have consented to that plan; but in application it will be diversified rather than general because it is grounded upon classification, and the immediate and primary problem of the secured landlord or claimant will be the problem of whether others, if any, and if so who, are to be classed with him so as to bind him by the action of two-thirds of the class. In this respect the Act provides that the court may direct the division of creditors and stockholders according to the nature of their respective claims and interests, and for the purposes of such classification may classify as an unsecured claim the amount of any secured claim in excess of the value of the security.

It may readily be seen that holders of bonds, debenture notes or other securities which are issued under the same mortgage, trust deed or trust indenture are apparently of one class, but beyond such situations there may be legitimate ground for classifying secured creditors into as many separate classes as the nature of the obligations and the differing character of the security reasonably permit. At least it behooves any secured creditor to assert himself in relation to his classifi-

cation so that he may not find himself drawn into a class in respect of which the plan makes provisions that may affect his interests to the advantage of others in the same class. The possibilities are much less that a landlord may find himself classed with other secured claimants, for each lease is usually unrelated to any other lease held by the same debtor, except in instances in which a joint building has been erected by the lessee on two or more adjoining parcels of leased land, and which might well permit of the lessors being all put into one class in view of their common relation to the security afforded by the joint building.

After the secured landlord and other secured creditors have seen to it that they are in a class of their own or in a class of other secured creditors whose interests will be most consistent with their own, their future status in relation to the proceeding will then depend upon whether the class, of which they are a part, assents to the plan by a two-thirds vote. If such assent occurs, the objector has no alternative other than to accept the provisions of the plan, since he is bound by the consent of his class. This proceeds upon the theory that as to any class of creditors, if two-thirds in amount consider the plan to be a sufficiently fair and proper protection of their interests, and the judge, as conditions of confirmation, finds the plan fair and equitable and not discriminating unfairly in favor of any class of creditors, and determines the plan to be feasible,—then minority objectors of any such class are not to be permitted to halt or obstruct the reorganization.

Equity reorganizations in the federal courts, confined chiefly to railroads, have in the past been without compulsion upon objecting claimants of any class, at least in legal principle and theory. There was no provision for compelling any objecting creditor of any class to go along with a plan of reorganization no matter how many others of his class might agree to it, but there was a practical compulsion in view of the fact that the receivership was based on a foreclosure suit, and the property would be sold under a foreclosure decree with an upset price fixed by the court, so that if a creditor did not choose to go along with the plan of reorganization he would simply be left out, and have his ratable participation, which might amount to little or nothing, in the cash proceeds of the sale. The right to bind an objecting creditor to a plan, which was not afforded by the former federal equity reorganization practice, is now supplied by the two-thirds majority rule, and the discretionary approval of the judge.

The other situation, yet to be considered, is that in which the secured landlord or creditor finds himself in a class of which two-thirds in amount have not approved the plan of reorganization. In that situation he is not required to go along as a party to the plan. These

instances are required to be dealt with in a way that will afford what the Act terms adequate protection for the realization by the creditor of the value of his lien or security.⁴ The plan itself may contain the provisions for that protection, but regardless of the plan the judge is authorized to provide that protection by any method he considers fair and equitable consistent with the circumstances of the case.

The particular situations which may arise in relation to the satisfaction of the claims of dissenting secured creditors or landlords, being those of a class not consenting to the plan, are innumerable, and not to be anticipated even in a very general way within the time limits of this discussion. Perhaps the best basis of discussion may be to take up now a few illustrative instances to which the principles provided by the Act are to apply:

First, in relation to the landlord: let us assume the debtor holds a lease with a considerable number of years to run on property devoted to some business purpose on which the lessee has constructed a building. As is usual, the lease requires the lessee to pay all taxes and assessments and a stated annual rental, and reserves to the landlord a first lien on the lessee's leasehold estate as security for all amounts required to be paid under the lease. The debtor is naturally desirous of continuing the lease as a primary condition of the reorganization, since the improvements on the leased premises not only represent substantial capital of the lessee, but there is a bond issue outstanding on the lessee's leasehold estate which has provided the bulk of the money represented by the building improvements. There are creditors holding chattel mortgages or conditional sales contracts upon some of the furnishings and equipment in the building, and also general or unsecured creditors.

Perhaps the first question the debtor will consider in framing its plan will be whether the landlord must be dealt with as a creditor by himself, or whether he may properly be classified with any other creditors, and if so, which ones, and the relative amounts of their various claims as compared with that of the landlord, so as to know what the possibilities are of the landlord's being drawn into a class of creditors, the consent of two-thirds in amount of which would bind him to the plan. But on the facts we have assumed it would not seem possible to properly classify the landlord with any other creditors. The nature of his demand is different, the nature and rank of his security are different, the remedies afforded him by law for protection of his rights and realization of his security are different. The one class to which he might be properly assigned would seem to be a class made up of another or other landlords owning parts of an entire site on which a joint building had been erected, or possibly a class made up of several

⁴ Section 77B (b), (4), 11 U.S.C.A. 207 (b), (4).

landlords if the situation were one in which the lessee held several leases of different locations, with a sufficient common relation by the terms of the leases and the nature of the business being transacted at the several places to warrant putting these landlords into one class. In the case we have assumed, however, there is only one lease held by the debtor. It would seem that the landlord is a class in himself and cannot be brought under the plan unless he consents to the plan, so good judgment on the part of the debtor would prompt it to arrange a plan sufficiently fair and reasonable to the landlord to warrant the hope that it could persuade the landlord to accept. The assent of the landlord in the case we have supposed is vital, for it can only be on the supposition of the continuance of the lease that other elements of the plan dealing with the leasehold bonds and other creditors can be worked out.

Is it possible in such a situation, if the landlord refuses to accept the plan, to carry forward nevertheless a plan of reorganization involving continuance of the lease by providing the dissenting landlord with the protection for realization of his security which the Act requires? It will be recalled that the Act requires in respect of each class of creditors who do not become bound by the plan, the provision, either in a method set up in the plan or as the judge may determine, of adequate protection for the realization of the value of their security. None of the modes suggested by the Act would seem to be appropriate to such a situation. For instance,—transfer or sale of the leasehold estate subject to the landlord's lien or retention of the estate by the debtor subject to that lien, would not disturb the landlord; neither would it afford relief to the debtor. Sale of the leasehold estate and transfer of the landlord's lien to the proceeds of sale, or appraisal of the value of the landlord's lien and payment of that amount in cash, which are the other suggested methods of affording the dissenting secured creditor protection, would seem inapplicable to such a situation. Those provisions are quite consistent with, and undoubtedly intended to relate to, the situation of a creditor secured by some form of lien or pledge, who, if he desired to realize on his security, would be required to foreclose by sale of the security, either out of court or through legal proceedings. Sale, either public or private, through proceedings in court or out of court, is the almost universal yardstick by which to measure and realize upon the value of the security, except possibly in a few instances such as land contracts or conditional purchases of personal property which permit of a forfeiture on the vendee's or purchaser's default. Perhaps it may be thought that this overlooks judicial determination or appraisal as a mode of valuation of security. It seems safe to say that judicial determination or appraisal as a mode of valuing security merely applies the measure of market or sale value. In troubled times such as now

obtain, when values thought to be normally present in property, find no adequate expression in the medium of exchange, it is natural to attempt some substitute expression by appraisal or other determination. The same expedient is resorted to in normal times, by way of fixing an upset price, when dealing with situations which preclude competitive bidding. But determination or appraisal, judicially made, relates to sale value, using immediate sales data if available, and if not resorting to data more remote, with such adjustments only as seem essential to reach the equivalent of a supposable bona fide offer of purchase.

But the landlord's position in the situation we have assumed is one quite different from all classes of other creditors holding a lien or security. It likewise differs from that of a vendor of real estate or a conditional vendor of personality; they have bargained away their beneficial ownership for a fixed price, retaining the legal title as security. The landlord has granted the use of his land for a term of years, conditioned on payment of the rent reserved at intervals concurrent with stated use periods, and with a lien on the granted estate for any default, together with a right of termination or forfeiture. Had he merely a lien with no right of termination or forfeiture his position in relation to delinquent rentals would then be comparable to that of a money demand creditor holding a lien or security in the ordinary way which he could only foreclose and realize on by sale of the lessee's estate. But the landlord's right to terminate the granted estate is not dependent upon or related to his lien. Unless lost by waiver it is a continuing power, and loss by waiver will rarely result, as the rather standard provisions of long term leases operate to avoid the rule in *Dumpor's Case*.⁵ Were the terms of such a lease of real estate transferred to any form of personal property the nature of the contract as mutually executory would be more readily apprehended, but our real property concepts have literally no base of origin or departure apart from the traditional estates; so the lessee's right is considered an estate, a term for years, as though it were an irrevocable entity. If the heritage of nomenclature be brushed aside, no justification would exist for viewing the relationship as other than an agreement mutually executory, the promise of the continued use of the land for the promise of continued payment of the compensation, apportioned in concurrent periods. Occasion for a realistic appraisal of the nature of the bargain does not frequently arise, but the incongruity of viewing it as a grant made in exchange for a debt created payable over a term of years, seems to have disturbed the judges when dealing with the question of the landlord's proving a claim for future rent or damages against a bankrupt lessee. Decisions denying the provability of such claims seem

⁵4 Coke, 119b (1603).

grounded on a rejection of the theory that the tenant's covenant to pay the stated rent was an acknowledgment in debt, and bring forward the view that consideration for the promise to pay for each rent period is the use of the land for that period.⁶ The Supreme Court of the United States recited this view without evidence of disapproval, but placed its determination on a wholly unrelated basis.⁷

The right of a lessor to terminate the lease when the lessee has failed to pay the rent is a forfeiture in name only. It is in fact nothing more than the lessor asserting a declination to be bound by his promise when the tenant has not fulfilled his corresponding promise. It is to be borne in mind that a plan which proposes continuance of the lease for the future assumes a value of the lessee's estate in relation to the plan, in excess of the rentals required to be paid. That excess value need not arise from a mere balancing of the stated rentals against the current or estimated future value of the use of the land. It may result from that or from the combined effect of peculiar relation of the site to the lessee's business or inability to realize or salvage in any other way than continuance of the lease, the investment of the lessee in building improvements. But whatever it be based on, the prediction of such an excess value seems an indispensable element of any plan involving continuance of the lease:—for the Act is not a disguised moratorium; neither is its design that of cushioning the fall of a corporation by ushering it gradually through ante-chambers of the bankruptcy court, when bankruptcy is evident as the eventual destination; nor does the Act include as a major premise any theory that the debtor is to be afforded a sporting chance of future success at present sacrifice of creditors' interests. There must be put aside as well the idea that the Act presents a liquidating mechanism by which, at the expense or risk of any one class of creditors, the corporation is to be nursed along until other classes of creditors may obtain a better realization. If continuance of the lease for the future has no such excess value in its relation to the plan, then the continuance seems necessarily discriminatory as against the interests of other creditors, and not likely to receive the approval of the judge. Once the assumption of excess value is indulged, the lessor's power of termination must be viewed accordingly. It is hardly to be anticipated that the Act will be so administered as to encourage inconsistencies.

The lessor's right of termination has been treated in equity as security. If considered as security it, doubtless, does not defy valuation. Yet its nature and functioning are such, when measured against an assump-

⁶ *In re Roth and Appel*, 181 Fed. 667 (C.C.A. 2nd, 1910); *Wells v. Twenty-first Street Realty Co.*, 12 F. (2d) 237 (C.C.A. 6th, 1926).

⁷ See *Manhattan Prop. v. Irving Tr. Co.*, 291 U.S. 320, 338, 54 Sup. Ct. 385, 75 L.Ed. 825, 833-834 (1934).

tion of substantial values to the lessee through continuance of the lease, as to warrant the conclusion that it is unlikely the court will say that adequate protection for realization of this security of the landlord will be given by offering the lessee's estate for sale or by appraisal of the value of the lessee's estate, and giving the landlord the amount thus ascertained to apply upon his delinquent rentals. So the opinion is ventured in relation to a situation, such as we have supposed, of delinquent rentals or other payments due under the lease, that the Act is not to be applied against such an objecting landlord by liquidating his power of forfeiture and thus compelling him to accept satisfaction of the past defaults on some basis less than their actual amount, coupled with continuance of the lease for the future.

Nor does it seem within contemplation of the Act that the dissenting landlord may be compelled to continue as part to a re-written lease which may scale down the rentals or change the other terms or conditions for the future years. The Act gives explicit authority, through the reorganization proceeding, to cause the rejection of contracts executory in whole or in part, including leases, but this appears merely an extension into the Reorganization Act of a comparable power previously existing under the Bankruptcy Act and in receiverships which recognized the right of repudiation or abandonment of what appeared to be burdensome executory contracts or leases. It is not thought that there is any basis in Section 77B to support the theory that, as against the landlord who has not become bound by the plan, the terms of his lease for the future may be recast and he made an involuntary party to the performance of such an executory undertaking over a future term of years on a basis wholly different from his lease and wholly different from what he is willing to contract. The suggestion of such a purpose in the Act would fall little short of the implication that any one having contractual relations with the debtor could be compelled to make new and executory contracts for the future. While Congress is not restrained from impairing the obligations of contracts as such, the Fifth Amendment guarantees due process of law when the federal power is exerted as a deprivation of liberty or property.

The conclusion would seem to be required that in the case we have assumed, our landlord, not being bound by the plan, will not be compelled to accept a reduced satisfaction of his claims and required to continue his lease in the future. While he may be unable to enforce his rights during the pendency of the reorganization proceedings, it is to be assumed that, regardless of the outcome of the proceedings, he will be afforded by the court a fair compensation for the use of his premises during the pendency of the proceedings, and when they are terminated, be left free to pursue his legal rights as he chooses.

An instance typical of what may be considered the other principal class of leases would be that of a lease held by a debtor running, say, 15 years or less, on all or part of a building in which the lessee had not made large expenditures for building improvements; a lease of store or business space, or all or part of a manufacturing plant. In such leases there may or may not be a lien for delinquent rents but there will always be the landlord's power of termination for defaults, as that power even though not reserved in the lease, arises through operation of proceedings for dispossession of the tenant on default in payment of rent. In leases of the kind referred to the lessee is not tied to the premises by large investment in building improvements, and under present conditions he could usually find a site perhaps as suitable on which to conduct the business and at a rental less than provided by the lease. In such cases continuance of the lease for the future, while sometimes desirable, may not be at all an essential element of a plan of reorganization. If it is not an essential element of a plan of reorganization, then the situation is the reverse of what we have previously considered and the landlord holds no dominating or key position which makes it essential that his consent to the plan be secured. The plan may contemplate the rejection of his lease either absolutely or conditioned upon his failing to consent to the plan. If he holds any security for the performance of his lease and his lease is rejected, his claims can be liquidated at the amount of delinquent rent or other payments then accrued under the lease at the time of the proceedings, plus his damages for the breach of the lease through rejection, which cannot exceed present value of the rent as reserved in the lease for the next three ensuing years. Should he hold any security for performance of the lessee's obligations under the lease that security can be valued in the manner provided by the Act, and should that security be of a kind that the debtor proposes to make use of in connection with carrying out the plan, such for instance as corporate stock of a subsidiary company, that security may be dealt with in one of the modes heretofore pointed out which the court may determine will give adequate protection to the security holder for realization of the value of the security, for instance, by requiring its sale at a fair upset price and transfer of the landlord's lien to the proceeds of the sale, or by appraisal of the value of the security and payment of that value.

In respect of such a landlord whose lease has been rejected and whose demands and damages under the lease have been liquidated, no question is presented of attempting to value the landlord's reserved power of termination of the lease such as discussed in relation to a situation where it was proposed as a necessary element of a plan of reorganization to continue the lease for the future. A landlord whose

lease has been terminated, whose demands and damages under the lease have been liquidated and who holds security would seem to be in no different position from any other secured creditor.

Having discussed the possibilities arising out of two typical instances of dissenting landlords having liens or security, let us consider some instances of the rights of other dissenting secured creditors. As previously indicated the secured creditor may, over his objection, be made to go along with the plan if two-thirds in amount of the creditors of his class approve the plan. The secured creditor has the same incentive as the landlord to avoid being drawn into a class with others. If he can possibly, by virtue of the nature of his demand or the character of the security he holds, properly ask to be classified alone, it will be advantageous for him to do so, for then he may determine without regard to what other creditors may do, whether he will or will not go under the plan, and without risk of being forced to go along over his objection. Since we are dealing primarily with the matter of satisfaction of the secured creditor who has not become bound by the plan, we must assume that, regardless of who he may be classed with, the class of our secured creditor has not given the two-thirds consent to the plan. Perhaps the most typical situations which will arise of secured creditors will be:

- (1) Those holding promissory notes or other money demands of the debtor secured by pledge of collateral; and
- (2) Those holding chattel mortgages or conditional sales contracts.

As an illustration of the first class, we take a debt, in whatever form, amounting to \$10,000 secured by pledge of collateral in the form of stocks, bonds or other securities. Since the creditor has not become bound by the plan he is entitled to adequate protection for the realization of the value of his security in one of the modes provided by the Act. It is unlikely in such a situation that, even though the collateral be of value considerably in excess of the debt, it would be practical to attempt a sale of the collateral subject to the pledge, although that is not impossible. Doing that would not seem to be of particular concern one way or the other to the creditor. It is more probable that in such a situation the attempt would be to have a sale of the collateral free from the lien of the pledge, and transfer of that lien to the proceeds of sale. Nor need the creditor be necessarily concerned over that mode of dealing with the security. He will simply be in the position that secured creditors are often in of attempting to bid the property high enough to prevent a sacrifice of his interests, knowing that his lien will be transferred to the proceeds of the sale. However, if the validity of the creditor's lien were in question and undetermined at the time such a

disposition of the collateral was to be made, he would hardly feel free to bid as much as though the validity of his lien against the proceeds of the sale was assured.

The third method suggested by the Act for protection and realization of the dissenting creditor's rights in the security is that of appraising the value of his interest in the security and paying him the appraised amount in cash. In respect of collateral which is not listed or has no ready market or readily ascertainable sale value,—measuring the value the creditor is to receive by an appraisal, may involve a great deal of speculation. Each case will depend on its own peculiar facts, but it seems entirely possible that such an appraised value might largely exceed any price which could actually be obtained by a sale, and it seems equally possible that such an appraised value might be a great deal lower than the creditor himself would be willing to bid in the protection of his interests at a sale. As against the possibility of a high appraisal there is the actuality that the appraised value must be paid by the debtor in cash out of moneys available in some form under the plan of reorganization, and it seems hardly probable that a corporate debtor requiring reorganization will be able to frame a plan providing sufficient cash to take over collateral at values much in excess of what could be realized by sale. The plan of the debtor presumably would be to require satisfaction of the claim through fixing a low value on the collateral especially if the collateral is of a nature, such, for instance, as stock of a subsidiary or affiliated company, as to have more potential value to the debtor in connection with future operation of its business.

In this connection it appears from the newspapers that the question has already arisen in a pending reorganization proceeding, whether the creditor could be compelled to take in cash the appraised value of the collateral he held, under the provisions of the Act which have been referred to, or whether he had the right to insist that the collateral be valued in the manner provided by Section 57 (h) of the Bankruptcy Law. The situation was one in which the creditor held as collateral to a money obligation the capital stock of a corporation which was a subsidiary or affiliate of the debtor, and the plan of reorganization proposed by the debtor had, as one of its elements, that the value of this collateral be appraised by the court and that value so determined be paid in cash to the creditor in satisfaction of his claim. The position of the debtor was that, having embodied this element in the proposed plan of reorganization, the plan supplied a mode of protecting the creditor's interest and for realization of his security in one of the ways permitted by the Act.

On the other hand, the position of the creditor appears to be that since one clause of the Act provides that in the case of secured claims

entitled to protection under the Act, the value of the securities shall be determined in the manner provided in Section 57(h) of the Bankruptcy Act, the valuation must be made in that manner.⁸ Section 57(h) of the Bankruptcy Act provides that the value of securities held by a secured creditor shall be determined by converting the same into money according to the terms of the agreement pursuant to which the securities were delivered, or by the creditor and the trustee, by agreement, arbitration, compromise or litigation, as the court may direct.

To this contention the debtor has answered that the appraisal method provided by its plan of reorganization is equally within the contemplation of Section 57(h) because the determination is made by the court after a hearing which is a determination by litigation within the meaning of Section 57(h), and that in any event the judge is given blanket authority by the clause of the Act which confers an overriding authority to determine, regardless of the plan of reorganization, a method which, in the opinion of the judge, will equitably and fairly provide the protection to be accorded the secured creditor. This issue has not yet been determined. It may not be of consequence in many cases, but it furnishes a good illustration of the debtor's framing his plan of reorganization so as to secure at an appraised price, presumably within the debtor's ability to meet, collateral which may have little sale or market value but may have a high utility value in connection with the future operation of the debtor's business; and the consequent position of the creditor who wishes to avoid having the collateral taken out of his hands at an appraised value, and would doubtless prefer the opportunity to outbid the debtor at a sale and then strike a bargain for future disposition of the collateral on terms of the creditor's choosing.

In most instances of dissenting secured creditors it will be of no great moment to the creditor what particular method of valuing and realizing on his security is proposed; for the measure applied will be directly or indirectly the market or sale value.

The other typical instance of secured creditors we have referred to is that of chattel mortgagees and sellers under conditional sales contracts. Since in Wisconsin and other states which have adopted the Uniform Conditional Sales Act,⁹ the seller who has received at least 50 per cent of the purchase price is deprived of the former right of forfeiture and required to sell the property at public auction, conditional sales contracts may be considered for practical purposes in the same category as chattel mortgages; both affording security only realizable through and measured by the results of a foreclosure by way of sale.

⁸ Section 77B (b), (10), 11 U.S.C.A. 207 (b), (10).

⁹ Wis. Stat. (1933) c. 122.

It will frequently happen that a corporate debtor seeking reorganization will have personal property, such as furnishings, equipment, machines and appliances, purchased on chattel mortgages or conditional sales contracts; and in instances of conditional sales contracts where more than 50 per cent of the purchase price has been paid and accordingly no power of forfeiture exists, the seller will stand much in the position of a chattel mortgagee, and the discussion will be upon that basis, referring for convenience to a chattel mortgagee. These situations will ordinarily differ from those of the secured creditor who has a money demand, with collateral pledged. The collateral is ordinarily not at all essential to the further continuance of the debtor's business and from the debtor's standpoint the matter of how the creditor's interest in the collateral shall be realized is ordinarily not of particular importance in framing a plan of reorganization. But chattel mortgages will frequently cover personal property which is rather vital to the continuance of the debtor's business and accordingly the debtor will make an effort to deal with it in the plan or reorganization. It is to be expected the debtor will ordinarily frame the plan of reorganization in such manner as to call for continuance of the use of the property, or sale of the property, subject to the lien of the chattel mortgagee, if the future use of the property is important in continuance of the debtor's business; but unless the mortgagee should have indicated in advance a willingness to go along on that basis, little would be accomplished, for the moment the reorganization proceedings had ended in court the mortgage would be in position, if his demands were not met, to enforce his security. If the debtor plans to be in position to take over the mortgaged property at a cash figure which would be a good buy for him, he may be inclined to provide in his plan that the value of the chattel mortgagee's lien be fixed by appraisal by the court and satisfied by a cash payment of that amount. This would present in practically the same form the same problems previously referred to in relation to a plan calling for the appraisal of the collateral and discharge of the pledge by payment in cash of the appraisal figure. If the chattel mortgaged property is not necessary to the continuance of the debtor's business but is of such a nature as to probably sell for a good price, the debtor will be more inclined to ask for a sale at not less than a fair upset price, and transfer of the lien to the proceeds of the sale, but there is ordinarily not a very profitable market for chattel mortgaged property which has been subjected to use. Usually only the seller or chattel mortgagee is inclined to bid more than a sacrifice figure. So unless the chattel mortgaged property is of such a nature in relation to the future continuance of the debtor's business as to prompt the debtor to make a fair provision for its future use under the plan of reorganization, the

chattel mortgage holder will be in a position quite comparable to that of a secured creditor holding collateral which the debtor has no desire to retain for future conduct of its business.

In dealing with all instances of secured creditors, whether holders of collateral, chattel mortgages or other lien, upon property which is not particularly needed for use in carrying the debtor's business forward under whatever plan of reorganization is proposed, it probably will not be of great consequence whether the valuation and realization of that security is to be worked out in one of the ways provided in Section 57(h) of the Bankruptcy Act or is to be worked out in one of the ways provided for protecting and realizing on the security of a dissenting secured creditor under the reorganization section. The principles developed in the administration of the Bankruptcy Act will undoubtedly be relied upon in that respect, and there seems no good ground for apprehending that such dissenting secured creditor will be subjected to any greater hazards than secured creditors have in the past under the Bankruptcy Act.

Federal equity reorganizations of the past, confined as they were principally to railroads and public utilities, were under the necessity of being carried through in some form, because of the public interest in maintenance of the utility service, but under the present amendment dealing with corporations generally, there is no such compulsion to carry through a reorganization; there is always the alternative of liquidation in bankruptcy.

This alternative, together with the discretion and authority conferred on the judge to confirm only a plan which he shall find to be fair and equitable and non-discriminatory and feasible in respect of future operation, are the important bulwarks upon which secured, as well as other creditors may rely in believing that no alleged necessity of continuing a business will be considered the primary factor and the interests of creditors a secondary factor, in administering the Act.

MARQUETTE LAW REVIEW

February, 1935

VOLUME XIX

MILWAUKEE, WISCONSIN

NUMBER TWO

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ROBERT W. HANSEN, LL.B. Marquette University Law School, 1933; member of the Wisconsin Bar. Former Editor-in-Chief of THE MARQUETTE LAW REVIEW.

HERBERT C. HIRSCHBOECK, LL.B. Marquette University Law School, 1921; member of the Wisconsin Bar. Assistant City Attorney of Milwaukee (1932-34).

HARRY R. McLOGAN, LL.B. Milwaukee Law School, 1909; member of the Wisconsin Bar. Present Commissioner, Wisconsin Industrial Commission.

PAUL J. MUNDIE, Ph.D. Georgetown University, 1930; ass't. Professor of Sociology, Marquette University.

CARL ZOLLMAN, LL.B. University of Wisconsin, 1909; member of the Wisconsin Bar. Professor of Law, Marquette University Law School.

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Published December, February, April, and June by the students of Marquette University School of Law. \$2.00 per annum. 60 cents per current number.